No. 90-972

IN THE

Supreme Court of the United States

October Term, 1990

BRUCE M. JONES, et al., Petitioners,

v.

EDWARD J. DERWINSKI,
Secretary of Veterans Affairs, et al.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

REPLY BRIEF FOR PETITIONERS

David M. Madway
David A. Leen
Bradford G. Moore
Counsel for Petitioners

Seymour Farber
Counsel of Record
1950 Addison Street
Berkeley, CA 94704
(415) 548-9400

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I. ARGUMENT

1. The Issues Presented are of Substantial Importance.

The Government attempts to minimize the importance of this case by noting that for VA guaranteed loans closed after January 1, 1990, recent statutory changes expressly preclude deficiencies (Br. in Opp. 6). That is small comfort to the thousands of California veterans who obtained VA guaranteed loans prior to January 1, 1990, and who have been, are being, and will be pursued by the VA for amounts claimed to approximate in excess of $200,000,000. That figure, provided by the VA some three years ago, is surely conservative in light of the enormous increases in foreclosures during the past two years. Moreover, Oregon and Arizona have anti-deficiency laws similar to California's, and class actions challenging the VA's similar position in those states are currently on appeal (*See* Pet. 5). And, of course, the VA will continue to collect these sums by administrative off-set regardless of any statute of limitations. *See* 38 U.S.C. 3114(c).

2. The Government Erroneously Interprets Congressional Silence. The Government argues that 1989 amendments of the VA legislation "implicitly" support the VA's attempt to collect deficiencies arising from foreclosures in California of 1989 and earlier loans (Br. in Opp. 6, fn. 6). But attaching significance to current congressional silence as a measure of what the law as enacted by an earlier Congress actually meant is sheer conjecture. Indeed, it is at least as reasonable to infer that by not expressly stating its intention to ratify the VA's interpretation of state anti-deficiency law protections, Congress intended to leave those protections in place for the pre-1990 loans. The Ninth Circuit agrees (*See* Pet. 5).

3. Application of California Law Does Not Constitute a "Grant". The Government quotes the *Shimer* language expressing concern that failure of the VA's "indemnity" rights against the borrower could convert the guaranty into a "grant" (Br. in Opp. 5). It is difficult to understand how anyone who has paid an insurance premium to the VA in connection with a loan (*See* 38 U.S.C. 1829), made payments on that loan, defaulted (in many

cases due to circumstances beyond the veteran's control, such as military transfer, illness, or job loss) and lost the home and equity in it through foreclosure, without any rights of redemption, can be regarded as having been the recipient of a "grant". The implication of unjust enrichment is not warranted, particularly since California's non-judicial process is among the least expensive and speediest in the nation to the special advantage of the foreclosing creditor.

4. California Law Does Not "Directly Conflict" with VA's Indemnity Regulation. Contrary to the VA's position (Br. in Opp. 6), California law does not "directly conflict" with VA's indemnity regulation, and it need not have been so construed. The regulation, 38 C.F.R. 36.4323(e), purports to obligate veterans for "[a]ny amounts paid by the [VA] on account of the liabilities of any veteran guaranteed..." under the Act (emphasis added). As noted in our opening brief (p. 14), under California foreclosure law, which the VA directs its lenders to follow, the veteran, following foreclosure of his home, is not liable to anyone, lender or guarantor. There is thus no conflict between

California's foreclosure law and the indemnity regulation. At best, the conflict is ambiguous and should not be resolved in a manner which prejudices California veterans. [1]

5. There is no "Indemnity Agreement".

Finally, the VA unfairly characterizes the form documents signed by veteran borrowers as "indemnity agreements" (Br. in Opp. 2). It is unseemly for the VA to engage in this sort of bootstrapping. In the applicable form, VA Form 26-1820, nowhere does it say "indemnity agreement". The language relied upon by the VA in that form relates solely to a situation where the borrower, without VA approval, sells the home to a third party who assumes the loan and then defaults. It recites that "This debt will be the object of established collection procedures." (Emphasis added.) The remainder of the paragraph, not quoted by the VA, emphasizes again the consequences of selling to

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[1] This court recently reaffirmed that in areas "traditionally occupied by the states, Congressional intent to supersede state laws must be clear and manifest." *English v. General Electric Co.*, ____ *U.S.* ____ *110 S. Ct. 2270, 2275 (1990). See also United States v. Church, 736 F. Supp. 1494 (N.D. Ind. 1990); United States v. Davis v. Derwinski,* ____ *F. Supp* ____ *(D. Minn. 1991).*

someone who cannot obtain new financing.

Even if this language were to be given the limited applicability required by its terms (i.e., to veteran borrowers who sell to assuming purchasers whose later default gives rise to a deficiency), the VA does not pursue for deficiencies only borrowers who sold houses to assuming buyers who defaulted. It pursues everyone, regardless of the cause of the default. Moreover, to a knowledgeable California borrower, "established collection procedures" means that recourse is limited to the security property, and that the borrower is not personally at risk. To a less sophisticated borrower, it is simply fine print gobbledegook.

There is thus no "indemnity agreement" in this case. The veterans have incurred no "obligations" under such "agreements". Whatever rights the VA has to recover deficiencies from California veterans can arise solely out of the claimed preemptive effect of 38 C.F.R. 36.4323(e), an ambiguous regulation, which itself is without a clear and necessary statutory anchor.

II. CONCLUSION

Various states have promulgated foreclosure laws that balance the interests of their citizens. Congress has directed that state foreclosure laws be used when there is a default on a VA guaranteed loan. This Court has been solicitous of state laws protecting debtors, particularly where property matters are involved. Accordingly, the VA, in using state foreclosure law, should comply with all state law requirements, not just those designed to benefit creditors.

For the reasons stated in the Petition and in this Reply the Petition for a Writ of Certiorari should be granted.

Respectfully Submitted:

Seymour Farber
Counsel of Record
1950 Addison Street
Berkeley, California 94704
(415) 548-9400

David M. Madway
David A. Leen
Bradford G. Moore
Counsel for Petitioners

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